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September 29, 1997

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Ex Parte Filing

William F. Caton, Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, D.C. 20554

In re Matter of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, **CC Docket No. 96-128**

Dear Mr. Caton:

On September 26, 1997, Jim Hawkins (BellSouth), Jeff Lamken and I met with Robert Spangler of the FCC on behalf of the RBOC Payphone Coalition to discuss issues in the above-captioned proceeding. The enclosed document was prepared by the Coalition and was used for discussion purposes.

Two copies of this letter are being submitted to you in compliance with 47 C.F.R. § 1.1206(a)(2) to be included in the record of this proceeding. If you have any questions concerning this matter, please contact me at (202) 326-7902.

Sincerely,

Michael Kellogg

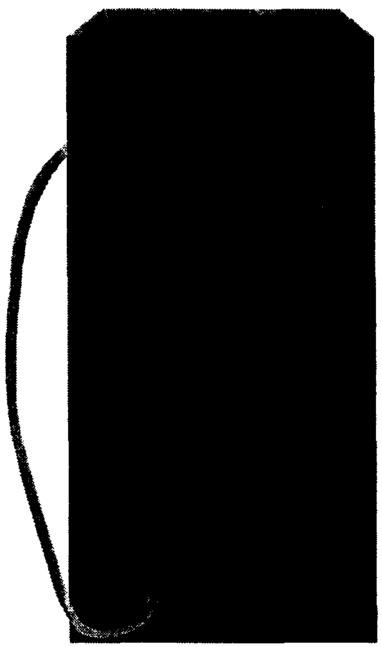
Michael K. Kellogg

Enclosure

cc: Robert Spangler

No. of Copies rec'd 0+2

Per-Call Compensation



RBOC/GTE/SNET
Payphone Coalition

Ex Parte Presentation

Sept. 26, 1997

Market-Based Rates

- **Market Prices Benefit Consumers**
  - Better services, lower costs, widespread deployment
  - Competition keeps rates down: "[I]t was not unreasonable for the Commission to conclude that market forces generally will keep prices at a reasonable level." <u>Illinois Pub. Telecom. Assn. v. FCC</u>,117 F.3d 555, 562 (D.C. Cir. 1997).
  - So does the threat of blocking: "[T]he market will address [relevant] differences and dictate appropriate per-call compensation amounts for each type of payphone call." <u>Recon. Order</u>, 11 FCC Rcd at 21268, ¶ 71; <u>accord</u>, <u>Illinois Pub. Telecom.</u>, 117 F.3d at 564.
- **Market Price *Is* the "Fair" Price**
  - "[T]he PSP will be providing a competitive service (payphone use) and should therefore receive compensation equal to the market-determined rate for providing this service." <u>Recon. Order</u>, 11 FCC Rcd at 21267, ¶ 68.
  - Where "competitive conditions exist, the most appropriate way to ensure that PSPs receive fair compensation for each call is to let the market set the price for individual calls originated on payphones." <u>Report and Order</u>, 11 FCC Rcd at 20577, ¶ 70.
- **Market Prices Adjust to Changing Conditions**
  - Accommodates "likely cost" and volume "variations" from region to region and "payphone to payphone." <u>Recon. Order</u>, 11 FCC Rcd at 21268-69, ¶ 71
  - Self-adjusting to changing economic conditions (<u>e.g.</u>, inflation, changing technology)

Court Did Not Reject Market-Based Approach

- **Court acknowledges that market pricing is appropriate**
  - "A market-based approach is as much a compensation scheme as a rate-setting approach." Illinois Pub. Telecom., 117 F. 3d at 563.
- **Court rejected only FCC's *cost* rationale for its choice of market proxies**
  - FCC chose local coin rate as proxy because the "costs" of subscriber 800 and access code calls were "similar" to local coin costs. 117 F. 3d at 563.
  - FCC did not address evidence that "the costs of local coin calls versus 800 and access code calls are not similar." 117 F.3d at 563.

Problems With Cost-Based Approaches

- **Cost-based approach does not equal "fair" compensation**
- **Cost-based approach either ignores widely different actual costs (among PSPs and in different states) or creates an administrative nightmare**
  - "We also reject arguments that we should base PPO compensation on the actual costs of the PPOs . . . Unless we are prepared to undertake the heavy burden of reviewing individual costs on an ongoing basis . . . this methodology would not be any more valid than a number of other approaches." Second Report and Order, 7 FCC Rcd at 3255-56, ¶ 32.
  - Costs of such a methodology are "completely disproportionate to any benefits offered by [the] approach." Second Report and Order, 7 FCC Rcd at 3256, ¶ 32.
- **Cost-based approach fails to support competitively-justified payphones with below average usage or above average costs**
  - "A cost-based compensation standard could lead to a reduction in payphones by limiting PSP's recovery of its costs, and this result would be at odds with the legislative purpose of Section 276 [to] 'promote the widespread deployment of payphone services to the benefit of the general public.'" Recon. Order, 11 FCC Rcd at 21267, ¶ 66.

Prevailing Deregulated Local Coin Rate is $0.35

Local Coin Rates in Deregulated States		
State	Deregulation Date	Prevailing Local Call Rate
Michigan*	November 1995	$0.35
Montana+	March 1990	$0.25
Iowa	September 1985	$0.35
Nebraska	January 1987	$0.35
North Dakota	August 1993	$0.35
South Dakota	November 1992	$0.25
Wyoming	March 1995	$0.35

* Informational tariffs still must be filed.

+ Detariffing applied to local calls only.

Avoided Cost Pricing

Costs of Dial-Around and Subscriber 800 Calls Versus Local Coin Calls		
Cost Type	**Mean Per-Call Cost Difference**	**Modal Per-Call Cost Difference**
Local Usage	-$.02	$.00
Coin Collection	-$.02	-$.03
ANI ii*	+$.05 TO $.08	+$.05 TO $.08
Uncollectibles (APCC)	+.03	+.03
Interest (APCC)	+.01	+$.01
Admin. Costs (APCC)	+$.01	+$.01
TOTAL	+$.06 TO $.09	+$.07 TO $.10

*If the Commission allows LECs to identify payphones using their choice of Flex ANI or OLNS technology, as contemplated in the Commission's OLS Order, see Policies and Rules Concerning Operator Service Access and Pay Telephone Compensation, 11 FCC Rcd 17021 (1996), payphone identification digit costs for the subscriber 800 and access code calls might be as little as $.01 per call. Coalition Remand Comments at 18 n.6; Andersen Remand Report at 7.

Per-Call Compensation Results (Summary)

Inverse elasticity/ Ramsey pricing	Local rate + $0.07 to $0.08 (minimum)	$0.42 to $0.43
Avoided/incurred Cost*	Local rate + $0.06 to $0.10	$0.41 to $0.45
Ad valorem tax	Local rate + $0.02	$0.43
Adjusted 0+ commissions (AT&T)	Local rate + $0.04 to $0.22	$0.39 to $0.57
Adjusted 0+ commissions (market)	Local rate + $0.08 to $0.28	$0.43 to $0.63

*If payphone identification digit costs are reduced to $0.01 or $0.02, as would occur if LECs were allowed to choose between Flex ANI and OLNS, the result would be the local rate plus $0.02 to $0.03, or $0.37 to $0.38.

Sources: RBOC/GTE/SNET Coalition Remand Comments at 23-24 (inverse elasticity); RBOC/GTE/SNET Coalition Remand Reply Comments at 15 (Avoided/Incurred Cost); RBOC/GTE/SNET Coalition Remand Comments at 23 n.10 (ad valormen tax); RBOC/GTE/SNET Coalition Remand Comments at 26 (Adjusted 0+ commissions); Comments of Peoples Tel. Co. at 21, 23-24 July 1, 1996 (IPP costs).

Flaws in AT&T Cost Study

- **Unrealistic cost estimates**
  - Ignores all but cheapest ($225) coinless payphone
    - Outdoor coinless stations cost $1,289.19
    - Average coinless card-type station costs over $900
  - Understates enclosure costs
  - Excludes fixed costs (information systems, billing, legal, accounting)
  - Excludes location costs (commissions/space rental)

- **Unrealistic total call counts**
  - Uses APCC not AT&T or Coalition numbers
  - Includes coin calls “made” from coinless stations

Flaws in AT&T Cost Study (Cont.)

- **Exaggerates cost differences between local coin and non-local coinless calls**
  - Local usage charge
    - Most lines flat rated
    - Loop costs non-traffic sensitive
  - Coin mechanism
    - Coin mechanism cost not "avoided" even if mechanism is not used
    - Coinless payphones only cost $35 per payphone, not $800 per payphone, less than coin phones. Andersen Report at 8. $35 difference, amortized over the life of the payphone, is too insubstantial to affect per-call cost
    - Smaller call volume on coinless payphones increases per-call cost
- **Corrected results: $0.42 to $0.41 per call (smart and dumb sets), and $0.84 per call (coinless phones)**